



May 14, 2008

Honorable David W. Combs
Members of the City Council
City of Rocky Mount
Rocky Mount, North Carolina

Dear Ladies and Gentlemen:

I am pleased to present and recommend this FY 2009 Operating and Capital Budget for the City of Rocky Mount. In accordance with North Carolina General Statutes, this recommended budget is balanced with respect to revenues and expenditures. Overall the FY 2009 Recommended Budget totals \$211,049,660. This represents a 6.9% increase of the FY 2007-2008 Adopted Budget of \$197,402,255, and a 3.4% increase of the FY 2007-2008 Revised Budget of \$204,145,402. This increase can be attributed to multiple factors, including increased material costs, expansion of services necessitated by annexation and continued commitment to public safety, debt financing of capital infrastructure projects in utilities to serve current and annexed residents, and implementation of a program to improve employee wages.

The proposed annual operating budget represents the financial plan for the following 10 funds, which include general government operations, public utilities, capital projects, and special allocations.

	<u>FY 2009</u>	<u>FY 2007-2008</u>		<u>FY 2007-2008</u>	
	<u>Proposed</u>	<u>Adopted</u>		<u>Revised</u>	
	<u>Budget</u>	<u>Budget</u>	<u>% Difference</u>	<u>Budget</u>	<u>% Difference</u>
General Fund	53,384,000	50,365,270	6.0%	52,078,781	2.5%
Powell Bill Fund	2,760,130	2,131,000	29.5%	3,305,700	-16.5%
E-911 Fund	250,000	390,000	-35.9%	390,000	-35.9%
Debt Service Fund	2,704,030	2,631,285	2.8%	2,631,285	2.8%
General Capital Fund	2,909,000	1,825,000	59.4%	1,832,000	58.8%
Electric Fund	86,888,500	83,321,365	4.3%	84,971,944	2.3%
Gas Fund	30,447,000	30,049,968	1.3%	30,220,654	0.7%
Water Fund	11,505,000	10,453,731	10.1%	11,046,356	4.2%
Sewer Fund	15,802,000	12,793,636	23.5%	13,483,002	17.2%
Stormwater Fund	4,400,000	3,441,000	27.9%	4,185,680	5.1%
Total	<u>211,049,660</u>	<u>197,402,255</u>	6.9%	<u>204,145,402</u>	3.4%

Where are we today?

Despite economic and operational challenges, we are pleased to report that continued, effective fiscal management has enabled us to function within the overall boundaries developed during the FY 2007-2008 Budget. Speaking in regards to general government, revenues from real estate property tax are projected to meet our budgeted levels, as are proceeds from our share of the state sales tax. Below budget projections for a small number of revenue sources, mainly fees for services provided by general government operations like inspections and recreation are offset by above budget collections for interest on City investments. Overall, general government revenues will match budgeted levels at the end of the current fiscal year.

Conservative management practices ensure efficient spending by all City services. While the cost of specific materials, notably fuel, have increased significantly in the past year, savings in other areas, such as salary vacancies, has provided the funds necessary to cover all expenditures while remaining below current budget levels. We anticipate ending the year with at least \$1 million in general government savings, which will ensure that our fund balance remains comparable with similar jurisdictions and the long-term financial responsibilities of the City.

Our utility enterprises have experienced mixed results in the past year resulting from significant external factors. Electric and gas operations continue to exhibit reasonably reliable performance, with sales levels meeting thresholds to ensure quality operations while covering necessary costs. Last year's drought did drastically reduce water and sewer usage, leading to a negative shift in revenues and requiring expanded use of fund balance to cover anticipated deficits and fund capital improvements that reduce the potential for future water shortages. We also anticipate savings in operations in both water and sewer as a result of planned expenditure reductions and some deferment of capital improvements. Also, our stormwater management program has established, consistent funding that enables provision of quality services and allocations for planned infrastructure projects.

The expanded commitment to community reinvestment established by the City Council in the 2007-2008 fiscal year has resulted in the identification of several projects designed to improve neighborhoods and foster enhanced economic opportunity for distressed local residents. Staff has started work on redevelopment of the Beal Street (Happy Hill) area and is preparing plans for Home Street (Southeast Rocky Mount), the Hale/Cotton Warehouse, and other areas. These represent the direction of the City Council towards neighborhood improvement and are in addition to existing projects involving the Downtown Streetscape and redevelopment of the Douglas Block area and Booker T. Washington High School.

Despite several notable episodes of extreme violence in the past year, the City experienced lower crime rates in the past year than in recent years. This is in large part due to changes in patrol and utilization of sworn officers, resulting in more officers on the street and the dedication of forces to the critical issues of weapons and drug enforcement. Our commitment to public safety also includes ensuring high quality fire and police services to areas part of the planned annexation on June 30, 2008. This required the addition of patrol officers during the current fiscal year in preparation for annexation taking effect.

Arrangements have also been made to secure firefighting services through a combination of service agreements with volunteer departments, improvements to supervisory staff to guarantee quality service delivery, and plans for the addition of a new fire station on the west side of the City in the near future.

The planned annexation also required additional work this year, much of which will continue over the next two months. Staff were added as part of the current budget to provide service in several areas, including community code and environmental services. These positions were budgeted to be filled and funded for the final part of the current fiscal year so they can be trained and prepared to provide the highest level of service to our new residents upon their introduction to the City.

Finally, the current year's budget included funding for a pay and classification study meant to evaluate current employee compensation and provide recommendations to improve pay and enable equity with respect to experience. Our entire staff participated in this study, which included a review of job descriptions, position pay grades, and funding levels. This study was conducted with the intention of funding approved recommendations in FY 2009. I will be sending the study recommendations to City Council in the next month or so for review and approval.

The challenges and opportunities faced by the City in the past year have tested our ability to maintain a healthy fiscal position. While we have achieved that task for now, the coming year poses additional challenges that require attention on the part of staff, the Council, and our residents.

Next Year's Prospective

Preparing the FY 2009 budget required substantial attention to several critical factors. Most notably, our current economic environment has created a situation where declining growth in revenues contrasts with the significant increase in the cost for essential supplies. Overall inflation is estimated at 4.4% for the past year, while specific materials, such as fuel and chemicals, have experienced price increases in excess of 30%.

At the same time, tightening of available credit and a worsening housing market have reduced consumer purchasing power on a national scale. The "lag-time" this region experienced in the past with respect to the implication of national trends does not exist in this circumstance, mainly because of the shift of our economic base from industrial production to consumer activity. While we do not anticipate the local real estate market experiencing a serious collapse, the overall impact of national influences could lead to some contraction in housing values as we approach property revaluation during the coming fiscal year. Retail sales may see some increase, but only in response to inflation for core purchases. As a result, corresponding tax revenues will not increase in a manner comparable with costs.

The City is projecting increases in revenue resulting from annexation. This includes property tax, sales tax, and household solid waste fees. While these revenues will help cover the cost of expanding services to new residents, increased costs will strain their ability to cover the expansion of government services necessary to provide an equal quality of service to new residents.

Reviewing current operations, staff also identified the need to examine those current and past expenditures funding with one-time revenue sources. Most notably, a \$500,000

increase in community reinvestment for FY 2007-2008 requested by Council was funded with one-time sources. In order to maintain this level of funding in order to match long-term priorities in this area of activity, we must also establish its position within the budget funded by current revenue.

Balancing the Budget

As a result of increased costs in the delivery of essential services and reduced revenue growth, staff faced serious challenges with balancing the budget for the coming year. Our first goal was to balance revenues and expenditures so that existing essential services were funded within the means provided by current revenue growth. We attempted to achieve this goal through the identification of more than \$2 million in department reductions in their budget requests, including the freezing of some vacant positions, deferral of projects to future years, and elimination of growth or actual reductions in other operating expenses.

These reductions enabled us to accomplish this goal in all areas except solid waste services. A 4.4% increase in our contract for disposal of collected garbage, along with significant fuel cost increases and debt service associated with recent purchases of replacement equipment, cannot be met with current revenue levels from solid waste fees. Therefore, I recommend a \$0.50 increase in the monthly residential solid waste fee, resulting in a revised rate of \$8.50 per month, and a 4.3% increase in fees charged by our transfer station.

Despite adjustments and offsetting reductions, we are still uneasy about funding for fuel purchases. We believe that additional funding, above the level provided by current revenues, is necessary to maintain existing service levels. This takes into account our continued efforts to reduce fuel use through existing and future conservation measures.

The next goal was to evaluate annexation-based revenues and balance corresponding expenditures in service expansion to these levels. Overall, we believe that this can be accomplished, though it will require careful evaluation in the coming months.

Finally, we worked on balancing to reflect additional necessary service expansions and inclusion of past appropriations funded with one-time sources. Unfortunately, we cannot achieve a balanced budget with current revenues and fund these initiatives. In order to provide a sustainable, annual funding source for these expansions, I recommend a \$0.03 increase in the property tax rate, resulting in a revised rate of \$0.58. This is a 5.2% increase that translates to \$45 for a \$150,000 home and \$7.50 for a \$25,000 vehicle.

This tax increase enables us to specifically fund the establishment of a permanent street engagement team to address drug and weapons enforcement. This team will be comprised of five new, dedicated officer positions. Funding is also needed to cover equipment, training, and other operations. Along with some additional funding to help cover salary increases for police and fire personnel and establish a fuel reserve, these expenditures represent \$0.015 of the \$0.03 tax increase.

The remaining \$0.015 of the increase provides the annual revenue source for community reinvestment. In the coming fiscal year, these funds will be used to cover the City's share of the purchase of property for the proposed medical arts building at Edgewcombe Community College, as well as provide funding for demolition of the

Hale/Cotton Warehouse, redevelopment of the Douglas Block and Tip Top Bakery and Planters Oil Mill properties, and to match allocation of federal community development funds for the residential redevelopment of the Beal Street (Happy Hill) neighborhood.

These tax and fee increases also keep in line with our policy of conservatively projecting revenues in the coming fiscal year. This leads us to attest that the financial plan for spending established by this budget can be implemented. Our monthly evaluation of revenues and expenditures, along with our constant monitoring of economic conditions, will enable us to identify potential circumstances where changes may be necessary, which will be achieved through spending reductions or appropriation of fund balance.

Revenue Overview

For the FY 2009 Recommended Budget, we expect the State shared revenues to continue to show little growth. Powell Bill revenue is expected to grow by 3-4%, utility franchise fees are expected to grow by 2%, beer and wine tax revenue is expected to grow by 2.5%, and the telecommunications tax revenue is expected to increase by 2%. No growth is expected for cable franchise fees, though we are adjusting the budget to reflect actual revenue performance. Sales tax revenue is projected to increase by about 2%. With most of these revenues, additional revenue will be made available as a result of the area and population included by annexation.

In Public Utilities, demand for both gas and electrical energy, as always, moves with the weather. The proposed budget does not contain either a gas or electric rate increase. As in past years, in the event our electric supplier adjusts its rates to the City, I would recommend continuing our practice of increasing or decreasing rates accordingly. The North Carolina Eastern Municipal Power Agency has, however, indicated that a rate increase is likely sometime later in the year. The City purchases gas on the market monthly. We will adjust our purchase gas adjustment, which is the cost-based portion of our rate, up or down in accordance with our cost of natural gas.

In addition to increases in water rates made during the adoption of the FY 2007-2008 budget, Council adopted additional increases to water and sewer rates in response to last year's drought. The budget reflects revenue levels made possible by current rates. Evaluating our rate structures in response to the drought, we believe changes need to be made so that rates reflect the sources of most use. We will be recommending at a later date a revised water rate structure that changes our current single rate for meters to a variable meter rate based on size. We hope that this recommendation will provide for reducing water bills for most of our residential customers.

The Stormwater Utility is operating well and no rate increase is requested. The fund is currently generating the funds necessary to cover operating cost and fund capital necessary for Stormwater system improvements.

Personnel

This year represents the second straight year where I am pleased to report that no increase will be necessary in employee health or life insurance premiums. Improved utilization of health services, including the implementation of the HealthMap Rx program, have helped control and reduce claims. Based on the best information available, our current plan provider is the best value. A team of employees is continuing to look into health improvement options and hope to report their results in the near future. We will

also continue to evaluate health insurance benefits offered to our employees and retirees in order to continue to provide a plan that is affordable to our employees and the City.

We are holding 25 vacant positions: 18 in the General Fund, 2 in Public Utilities, and 5 in Water Resources. Many of these positions have been held vacant since the spring of 2001 when the State first withheld funds from the city. Several new holds are for part of the coming fiscal year and will be filled in a fiscally responsible manner.

This recommended budget provides for the addition of 21 new positions, with 11 in the General Fund, 5 in Public Utilities, and 5 in Stormwater. Among the new positions are 4 Police Officers and a Corporal for the Street Engagement Team and 3 Battalion Chiefs in the Fire Department to ensure service delivery with annexation. The budget also requests moving the current part-time Administrative Clerk position in the Fire Department to full-time, along with additional positions for Finance, Engineering, and Planning.

I have included funds for pay for performance increases for employees. I continue to believe that this program demonstrates that our employees are our most valuable assets. This program is essential to retaining employees and encouraging their improved performance. We have also allocated fund balance in order to implement recommendations from the comprehensive compensation study once they are approved by Council. We anticipate that implementation will occur on October 1, 2008, in order to provide time for effective evaluation and review of employees and their positions with respect to the recommendations.

Capital

During the process of developing this year's Capital Improvement Program, we identified priorities for capital projects and kept our focus on funding those specific initiatives. This allowed us to proceed through the Operating Budget process without making significant reductions in funding already presented to the Council in March. While some reductions are necessary, the Capital Budget for FY 2009 is very similar to what has already been presented.

A priority in capital expenditures is to provide funding to adequately complete and equip projects that are already underway or committed to. Included in this priority are projects in all of the utility funds that accomplish needed multi-year upgrades and repairs, a continued commitment to timely Police vehicle replacement, and funds to continue downtown revitalization, including the Douglas Block.

There are also some projects that have been deferred in the past and now require action. Debt proceeds will enable us to replace the roof of City Hall, renovate the Headquarters Fire Station and Life Safety Building, and replace the HVAC system at the Senior Center.

General Fund/General Capital Fund

The following are some programs and services funded through this budget. For the most part, budget requests supporting existing programs and services were funded. As is always the case, there are more needs than current resources can support, especially in the General Fund. In some instances, small increases were included when necessary and needed. We carefully reviewed capital requests and limited funding of these items.

As you review the budget, you will note some increases in operating costs. The cost increases the City must cope with are similar to items that every business and household experiences, but frequently the City's costs are a larger portion of its total budget, reflecting the nature of local government operations. These areas include communications, utilities, gasoline/diesel fuel, and chemicals.

Funds are included for the replacement of ten patrol cars in the Police Department, as well as the purchase of additional cars to accommodate the street engagement team. This expenditure is part of a capital project included in the CIP. This is the sixth year of a process of patrol vehicle replacement, made necessary because of the continuous high mileage accumulated on patrol vehicles. The Police Department must have a dependable fleet of patrol vehicles to maintain a consistent presence in neighborhoods and to respond to emergencies.

This year, we are providing funds to initiate the planning and design of a new fire station on the west side of the City. This facility will be constructed in the next five years and will enable the Fire Department to provide service with response times in existing and annexed territories at levels comparable with the rest of Rocky Mount. At this point, we are still working with Nash Community College on securing a location for the station, possibly as part of a regional public safety training facility operated by the college.

Several projects proposed in the CIP are scheduled for funding in the coming year, but are not included in this proposed operating budget. These projects are multi-year in scope and depend heavily on funding sources outside the City. Therefore, they will be funded, but submitted to the Council as project ordinances for adoption at the same time as the budget. They include the Downtown Streetscape, redevelopment of the Douglas Block, Booker T. Washington High School, and the Beal Street (Happy Hill) neighborhood, as well as the construction of Battleboro Park.

Powell Bill Fund

This Recommended Budget provides for Powell Bill projects totaling \$2,760,130. In the upcoming year, we expect to receive \$2,025,000 in Powell Bill revenue, a 5.3% increase in the actual FY 2007-2008 revenue for streets and roads projects. We have budgeted \$900,000 for street resurfacing. The budget also provides continuing funding for new construction and repair of sidewalks.

We will continue to make contributions from Powell Bill to both the General Fund and the Stormwater Fund to cover Powell Bill eligible activities such as crack sealing and asphalt patching in the General Fund and ditch maintenance and street sweeping in the Stormwater Fund. These contributions have been reduced, however, to make more funding available for capital projects.

Electric Fund

Funds available in the Electric Fund are directly related to the relationship between sales and purchases. The largest revenue and expenditure in the city budget is for the sale and purchase of power. Utility sales and purchases are anticipated to be in line with actual performance this year. The Recommended Budget does not include an electric rate increase.

The Electric Budget includes the normal electric operating expenses such as supplies, equipment maintenance and repair, and fuel. The cost of these items is increasing. The budget also includes funding for an additional Lineman, Load Management Technician, Lead Dispatcher, and two Dispatchers. The dispatcher increases will enable the expansion of utility dispatch operations to 24/7 service.

The Capital Budget has not been reduced from what was recommended in the Capital Improvement Program. Among other projects, this recommended budget includes funds for distribution system improvements (\$250,000), transmission pole replacement (\$200,000), and funds for continuation of the automated meter-reading project (\$150,000), an effort that will be undertaken by all the utility funds.

Gas Fund

The Recommended Budget does not include a gas rate increase. In the event the City's gas supplier adjusts its rates, I will recommend we continue the City's practice of adjusting rates accordingly.

The capital projects in the Gas Fund include the cost of new lines (\$300,000), providing new service connections (\$150,000), continuing the cast iron main replacement program (\$250,000), and funds for the automated meter reading project (\$100,000).

Water Fund

The revenue deficit resulting from the reduction in water usage caused by last year's drought necessitates utilizing a significant amount of fund balance in order to balance the current year. Therefore, in order to prevent further erosion in the fund balance, we have eliminated any appropriation as part of the FY 2009 budget. (Revenue levels reflect the current rate structure, as well as the proposed rate structure if implemented by Council, which is revenue neutral).

Capital projects in the water fund include hydrilla management (\$50,000), existing system improvements and repairs (\$405,000), and automated meter reading (\$200,000). Additional projects will provide for extension of lines to annexed areas (\$536,000).

Sewer Fund

As with water, no fund balance has been appropriated for the FY 2009 budget as a result of the need for additional resources in response to last year's drought. Revenue levels reflect current rates, which were adjusted earlier this year.

The Sewer Fund budget includes the normal expenses for operating and maintaining the sewer systems and plant. This year funds the second round of several significant extension projects associated with responding to development and annexation. These

particular projects will be funded with debt, which will place additional pressure on the fund in the future, though revenue may offset to some degree growth due to an increase in customers. Capital projects will include extending mains (\$4,285,000), continuing the rehabilitation of existing mains (\$150,000), and expansion and improvements to pump stations (\$475,000).

Stormwater Fund

The recommended budget includes the addition of a maintenance crew (4 positions) to expand service to annexed areas and an administrative clerk. Capital funds are appropriated for continued work in the Eastern Tar/Gay Branch area (\$500,000), additional improvements (\$520,000), and stormwater inventory of annexed areas (\$140,000).

Final Thoughts

Rocky Mount faces significant challenges in the coming years to provide a high quality of essential services to its residents while undertaking initiatives designed to improve the quality of life of its challenged or distressed residents. Increased material costs will require us to improve efficiencies and rethink operating practices to achieve some degree of offset, but when combined with expanding our involvement in community reinvestment, a greater revenue base is necessary. Funding the recommended budget without increasing the revenue base will require continued allocation of one-time funds, endangering our financial health, or making important decisions on the priority of current and proposed services provided by the City.

Conclusion

I am pleased to present this budget, which I believe to be in keeping with City Council's immediate goals and objectives. I anticipate in this coming year that we will see volatility in the City's business activity and residential development, with the potential for both decline and growth. While we do not have the flexibility we once enjoyed, I believe this budget positions the City where it needs to be for the coming year, and I recommend it for your approval.

Thank you for your consideration of this budget. I look forward to reviewing and discussing it with you.

Sincerely,



Stephen W. Raper
City Manager

